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UNCLAS SECTION 01 OF 02 BAGHDAD 001328

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STATE FOR NEA-I, EEB

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TAGS: [ECON](#) [EPET](#) [ENRG](#)

SUBJECT: OIL MINISTRY RESPONDS REGARDING IN-KIND PAYMENTS  
FOR TECHNICAL SERVICE AGREEMENTS

REF: A. A) STATE 36481

[B. B\) BAGHDAD 1021](#)

[C. C\) STATE 41382](#)

[1](#)1. (SBU) SUMMARY: The Ministry of Oil sent us the proposed text of the payment terms of its technical service contracts, explaining the proposed transaction is structured as an accounting offset, in hopes of securing USG approval of its proposed payment scheme. Post requests guidance on the draft text. END SUMMARY.

[1](#)2. (SBU) We shared the text of ref A with the Director General of Contracting at the Ministry of Oil, and followed up with discussions on April 16 with his deputy, Abdul Mahdy al-Ameedi, regarding USG concerns about the proposed payment mechanism for the technical service contracts for oil field development. Mahdy's initial reaction was "we know that we are under an occupation, but what law prevents the GOI from establishing this type of contract, which is quite common in the industry?" The contracts involve large transfers that the Ministry of Finance would not be able to support, and, he added, the well-known failings of the Iraq procurement system represent another obstacle which alone should warrant acceptance of the Iraqi work-around. We suggested that the proposed contract language be presented for USG consideration, and another meeting held if needed to discuss possible solutions.

[1](#)3. (SBU) On April 27, the DG, Natik al-Bayati, wrote a lengthy message to allay USG concerns regarding the proposed in-kind payments to international oil companies (IOCs) for technical service contracts. Bayati explained that all of the IOCs have contracts with the State Oil Marketing Organization (SOMO) for monthly purchases of crude oil and that the MOO would deduct the dollar amount of an IOC's TSA invoice to the MOO from SOMO's crude purchase invoice to the IOC. The IOC would thus purchase crude oil in the ordinary course of business but reduce the amount it pays SOMO for a given quantity of oil by the amount the MOO owed the IOC for services recently rendered and invoiced under the TSA. This procedure, Bayati explained, is all that is meant by "in-kind" payments.

[1](#)4. (SBU) Bayati further explained that SOMO could calculate Iraq's payment to the United Nations Compensation Commission (UNCC) using 5 percent of SOMO's gross revenues for crude sales, i.e., before the reductions from the amounts paid by the IOCs for their crude to recognize their services rendered under the TSAs. Bayati also advised that all the documents and invoices could be audited by internal and international auditors, such as Ernst and Young, consistent with practices under UN Security Council Resolution 1483. Bayati noted the MOO would keep the Finance Ministry well informed, and copied the proposed contract language for our review.

15. (SBU) ACTION REQUESTED: We have forwarded the correspondence from Bayati to the Department for guidance regarding whether the above clarifications and assurances adequately address Washington agencies' concerns about in-kind payments for services under the TSAs. In our view, the relevant contractual language should address those concerns, albeit perhaps with some textual modifications. Post would greatly appreciate a review by Washington agencies of the contract language as soon as possible, as we plan to meet with Minister of Oil Shahrastani next week.

16. (SBU) The relevant draft contractual language provides the following:

BEGIN CONTRACT TEXT

9.1 For the performance and completion of the Services in accordance with the Contract, SOC shall pay or cause to be paid to contractor, at the times and in the manner specified in this Article, the remuneration defined in Annex B-Rates and Prices.

9.2 Unless it is specified otherwise in the contract, Contractor shall submit to SOC and SOMO each calendar month (quarterly) a duly documented invoice covering the fees for the portion of the Services performed or completed and for reimbursable items procured during the preceding calendar month (quarter), SOC may deduct from any payments to be made to contractor any undisputed amounts contractor may owe to SOC under the contract.

9.3 The value of any invoice will be deducted from the value of SOMO's commercial invoice under any existing crude sales

BAGHDAD 00001328 002 OF 002

contract with (Contractor). Such deduction shall be made by SOMO from the invoice relating to the next shipment of crude oil lifted by (Contractor) after receipt by SOMO of the said Invoice. This arrangement shall be subject to (Contractor) and SOMO having confirmed their agreement by letter, substantially in the form of Annex (...)

9.4 In the event SOC disputes an amount invoiced, SOC shall notify contractor thereof within thirty (30) Days of the receipt of such invoice specifying the reason thereof. SOC shall pay or cause to be paid the entire amount of the invoice including the disputed portion within such thirty (30) days period from the said notification. The parties shall use all reasonable endeavors to expeditiously settle such dispute, Contractor shall pay back SOC the amount due to SOC, if any, which amount shall bear interest at LIBOR US Dollar ( 0) from the date of payment of the invoice.

9.5 Any overdue payment by either party to the other hereunder shall bear interest at a rate specified at the published LIBOR one-month rate on the due date.

END CONTRACT TEXT  
CROCKER